

MARKET UPDATE

JUNE 10, 2022

INFLATION PEAK?

Today's May 2022 monthly inflation readings were not quite what some had hoped for, at least those that thought the April readings were the peak. The consumer price index (CPI) rose 8.6% in May from a year ago, the highest increase in over 40 years. Core inflation, which excludes the impact of food and energy, rose 6%. Both were slightly higher than expected. So, what does this mean? The biggest impact will be the response of the Federal Reserve. The minutes that were released a few weeks ago indicated that Fed officials are prepared to move ahead with multiple 50 basis point interest rate increases. Does today's inflation data cause them to change their path? I don't believe so. But both the stock market and the bond market are now pricing in a chance they turn more hawkish. Hence why US stock markets were down 5% this week and the 10-year US Treasury rate was up 15bps on the week.

Investors and markets are watching two very important upcoming events; June 14-15 is the next Fed meeting followed by the usual press conference. The action taken, as well as the forecast for future action will be watched closely. And July 15 begins the Q2 2022 earnings season. However, leading up to this, we are bracing for a wave of negative preannouncements before the Q2 earnings reports begin. Analysts expect earnings growth of 4.8% for Q2 2022, 10.6% for Q3 2022, and 10.1% for Q4 2022. And for the full calendar year 2022, analysts are predicting earnings growth of 10.1%. I am not quite sure that the market believes these numbers, which is why we expect some negative revisions. However, some of this is already priced into the market. The key question will be; how much downward guidance do we get? The next few weeks will give us a good idea.

As I had mentioned in my last update, there are valid reasons why some folks on the Street are calling for a recession either late 2022 or early 2023. Interest rates are rising, and growth is slowing. Yes, the Fed will take aggressive action to raise rates and attack inflation. But we continue to believe that the economy can grow even with the series of rate hikes ahead. A hard-landing recession seems less likely than the other scenarios, given the economy is at full employment and supply channels are filling back up. Time will tell, but we are confident that both monetary policy, along with natural market supply/demand factors will engineer a new baseline of inflation and growth in which markets will be priced. Our portfolios continue to be positioned with short duration in Fixed Income and an overweight to US equities vs. International with a Value tilt.

Regards.

Jason



Jason Kass, CFA, CFP®
Chief Investment Officer & Sr. Portfolio Manager
Legacy Edge

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